

**“China’s Proliferation and the Impact of Trade Policy on
Defense Industries in the United States and China”**

Testimony before the U.S.-China Economic and Security Review Commission

by

**Ambassador Don Mahley, Deputy Assistant Secretary of State for
International Security and Nonproliferation
Washington D.C.**

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Mr. Chairman and Commissioners of the U.S.-China Economic and Security Review Commission, thank you for the opportunity to appear before you today and discuss China’s nonproliferation practices, their impact on U.S. national security, and how to improve China’s nonproliferation record. My name is Don Mahley, and I serve as Acting Deputy Assistant Secretary of State for International Security and Nonproliferation, the bureau whose mission it is to lead U.S. diplomatic efforts to prevent the spread of weapons of mass destruction, their means of delivery, and advanced conventional weapons.

The Nonproliferation Agenda

Mr. Chairman, the President is committed to working toward a relationship with China that enhances America’s security, China’s concerns, and the security of our friends and allies. To that end, we continue to engage China on nonproliferation matters in a constructive and candid manner. As the President stated during the visit of President Hu Jintao on April 20, 2006:

Prosperity depends on security – so the United States and China share a strategic interest in enhancing security for both our peoples. We intend to deepen our cooperation in addressing threats to global security – including the nuclear ambitions of Iran, the genocide in Darfur, Sudan, the violence unleashed by terrorists and extremists, and the proliferation of weapons of mass destruction.

The President has been clear in his desire to work with China to address our common nonproliferation agenda and has made this an important part of the bilateral relationship and our overall nonproliferation strategy. We continue to work with China to expand our areas of common interest and to improve our existing cooperation on nonproliferation. However, the U.S. continues to have serious concerns about the proliferation activities of certain Chinese entities and we continue to take action in response to these activities. We have worked productively with China on a number of important proliferation issues, yet we also have made it clear that China can, and should,

be doing more to halt the spread of WMD, missiles, and conventional weapons and related technologies.

Chinese Export Controls

Over the years, China has taken a number of steps to improve its export controls. China, a party to the Nuclear Nonproliferation Treaty, the Biological and Toxin Weapons Convention (BWC), and the Chemical Weapons Convention (CWC) has also become a member of the Nuclear Suppliers Group (NSG) and the Zangger Committee. In 2002, China adopted export controls similar to the Australia Group control lists on chemical and biological related items and technology. In addition, in August of 2002, China promulgated comprehensive missile-related export controls that approximate those of the Missile Technology Control Regime. In November and December of 2006, China's State Council approved two sets of revised export control regulations that harmonized China's nuclear export control regulations with the Nuclear Suppliers Group (NSG).

China also has produced two official white papers outlining Chinese nonproliferation policy. The December 2004 *China's National Defense in 2004* and the September 2005 *China's Endeavors for Arms Control, Disarmament, and Nonproliferation* stated China's opposition to the proliferation of weapons of mass destruction and their means of delivery and outlined China's commitment to support the international community's effort to stem such proliferation.

These are steps in the right direction that this Administration supports.

Chinese Cooperation on North Korea and Iran

China has played an increasingly positive role in responding to some of the world's most pressing proliferation problems. Nowhere is that more evident than with regard to the North Korean nuclear program. As you know, China has long had a close relationship with North Korea, and for decades was a key source of military technology and hardware. However, following North Korea's provocative missile launches of July 2006, and its October nuclear test, China joined in the Security Council's vote to enact strong measures under UNSCR 1695 and UNSCR 1718. With these resolutions, China has sent a message to North Korea that it must agree to the complete, verifiable and irreversible elimination of all of its existing weapons of mass destruction and ballistic missile programs. With its vote for resolution 1718, China supported the imposition of sanctions under Chapter VII of the UN Charter requiring all Member States to prevent the transfer to North Korea of WMD, ballistic missiles, a broad range of conventional arms, and related items, and prohibiting North Korea from exporting those items. UNSCR 1718 also requires Member States to freeze immediately financial assets that are owned or controlled, directly or indirectly, by persons or entities designated by the Security Council or the 1718 Sanctions Committee as being engaged in or providing support for North Korea's WMD and ballistic missile programs. UNSCR 1718 also requires Member States to prevent the transfer of luxury goods to North Korea.

Beijing has served as host to the Six-Party Talks, and has played a constructive role in the September 2005 Joint Statement, where North Korea committed to abandoning all nuclear weapons and existing nuclear programs and returning to the NPT and to IAEA safeguards, and the subsequent February 13 Initial Actions agreement, where North Korea committed to “shut down and seal for the purpose of eventual abandonment the Yongbyon nuclear facility, including the reprocessing facility, and invite back IAEA personnel to conduct all necessary monitoring as agreed between the IAEA and the DPRK.” As we now begin the process of ensuring that North Korea honors its commitments, Chinese support is absolutely essential in maintaining a united front.

It is worth noting that, while the focus of the Six-Party Talks is on denuclearization, these talks are establishing an important precedent for multilateral cooperation on proliferation matters around the world. For example, the February 13 Initial Actions Agreement formed a Working Group on a Northeast Asian Peace and Security Mechanism, which we hope will develop strategies to further regional cooperation.

With regard to Iran, China shares our goal of preventing Tehran’s acquisition of a nuclear weapons capability. In June 2006, China joined with the other Permanent Members of the Security Council and Germany in offering a generous package to Tehran in exchange for it suspending its proliferation-sensitive nuclear activities and entering into negotiations. Although that offer remains on the table, regrettably Iran has refused to accept. China has been a reluctant supporter of sanctions as a mechanism to increase pressure on Iran. However, China, in response to Iran’s failures to comply with its obligations, did join the rest of the UN Security Council in the unanimous adoption of Chapter VII sanctions in UNSCR 1737 and UNSCR 1747. These resolutions prevent Member States from supplying Iran with certain items, technology, training or financial assistance that could contribute to Iran’s nuclear program or its development of a nuclear weapon delivery system. The resolutions also require States to freeze certain financial assets of entities identified in the Annexes of the resolutions as having a significant role in Iran’s nuclear and missile programs. China has also joined with the P5+1 in reiterating that should Iran continue to refuse to walk down the path of negotiations, additional sanctions will be necessary to augment those already in place.

We expect all States, including China, to implement fully and effectively their obligations under UNSCRs 1718, 1737 and 1747, and we maintain an active dialogue to support the universal implementation of these resolutions. The entire international community, including China, must be unified and consistent in its message to North Korea and Iran that those two countries cannot hope to engage in business as usual until international concerns regarding their nuclear and missile ambitions have been resolved.

Continued Outstanding Concerns

China’s nonproliferation record is improving gradually, but some Chinese entities continue to supply items and technology useful in weapons of mass destruction, their means of delivery, and advanced conventional weapons programs of concern, despite the UN Security Council resolutions, I just mentioned. China has some important

deficiencies in its export control system that it needs to address, particularly in enforcement and implementation, and, possibly, willingness. We still observe Chinese firms and individuals transferring a wide variety of technologies to customers around the world – including to Sudan, Burma, Cuba, Syria, and Iran.

Mr. Chairman, you asked that I address the question of the extent to which the Chinese government is knowledgeable of and participating in proliferation activity. Certainly we have witnessed over the years an improvement in the behavior of the Chinese government and its ability and willingness to prevent proliferation sensitive transfers to countries of proliferation concern. Nonetheless, Chinese companies, including some state owned enterprises continue to proliferate despite repeated notifications and discussions by the United States with Chinese officials. The extent to which the Chinese government or Chinese officials are witting of the proliferation activity of non-state owned Chinese entities is difficult to estimate. We do know that economic decentralization is a key feature of China's economic reform. However, we simply do not know enough about the practical, every day workings of the decision-making process or structure of China's export control regime to ascertain the level of control or awareness that Chinese officials have over increasingly free-wheeling Chinese companies that trade in materials related to WMD and their delivery systems. Nor do we understand the extent to which the Chinese government may be witting in the exports to certain countries. These transfers remain a serious concern, and we will continue to press Chinese officials to act vigorously to investigate and enforce their export control regulations.

Chinese firms have continued to supply Iran with a range of conventional military goods and services in contravention of the restrictions within these resolutions. The United States has sanctioned a number of Chinese companies under the Iran and Syria Nonproliferation Act for the sale of items on multilateral control lists or items with the potential to make a material contribution to ballistic or cruise missile programs or WMD programs. Nine Chinese companies currently are under ISNA sanctions. The three Chinese entities to be sanctioned most recently (April 2007) include:

- China National Precision Machinery Import/Export Corporation (CPMIEC);
- Shanghai Non-Ferrous Metals Pudong Development Trade Co. Ltd.; and,
- Zibo Chemet Equipment Company.

The continued imposition of sanctions on Chinese entities clearly shows that China needs to do more to ensure effective and consistent implementation and enforcement of its export controls. With specific reference to conventional weapons, China, like many other countries, views its trade in conventional weapons as helping nations to meet their perceived defense needs and notes that there are no international agreements preventing these sales. China makes this assertion, despite evidence that Iran has transferred weapons to Shia extremists in Iraq terrorist groups and to Hizballah and the Taliban. China appears generally to accept end-use assurances it receives from countries that purchase Chinese arms, including from countries such as Iran, Syria, North Korea, or Sudan. Nevertheless, China has demonstrated sensitivity to growing international concerns about recipients of some of its arms sales, notably Sudan. China's recent

designation of an experienced senior diplomat as its special envoy for African issues, with an emphasis on Sudan, is an encouraging, positive step. We maintain an active dialogue with China about conventional weapons transfers, and will continue to seek greater cooperation in curtailing transfers to state sponsors of terrorism and in stricter and more uniform application of export control safeguards.

China must do more to bring the enforcement of its export controls up to international standards. It needs to implement effectively its export control regulations and rein in the proliferation activities of its companies. It needs to address continuing deficiencies in its system, particularly in enforcement, holding violators accountable. China needs more uniform implementation of its export controls, including its catch-all controls, particularly for missile related transfers, and needs to be more willing to share information on actions the government has taken in response to U.S. demarches. We will continue, as warranted, to impose sanctions against Chinese companies engaged in proliferation and highlight our ongoing concerns about China's proliferation record with the Chinese government.

Areas of Cooperation

Sanctions remain a deterrent tool in the U.S. nonproliferation toolbox. But we also seek to make China a willing partner in addressing our common proliferation concerns by engaging cooperatively in a number of areas. To this end, the U.S. will continue to urge China to revise its policies and practices to meet international standards.

Over the past few years, the United States and China have begun working together to further our nonproliferation objectives. We are working to maintain a line of communication, permitting both sides to exchange views and concerns in a frank and candid manner. In particular, we regularly discuss with China our concerns about certain proliferation-related activity. It was a subject when the President met with President Hu in April 2006. It was a topic when Deputy Secretary Negroponte met with Chinese Executive Vice-Foreign Minister Dai Bingguo just last month. The Department of State also serves as the American lead on an ongoing Nonproliferation Dialogue with the PRC, led at the Assistant Secretary level, and also a Strategic Dialogue, led at the Undersecretary level.

Chinese officials have indicated that they welcome the discussion of these specific activities and report to us that they regularly investigate, based frequently on our information, to ascertain whether Chinese companies are not violating Chinese law or relevant UN Security Council Resolutions.

Beyond discussing our shared interest in preventing proliferation, there are a number of instances where the Chinese have expressed an interest in export control cooperation, including technical exchanges and training. To the extent that it is permissible within the law, we have endeavored to provide such assistance.

One such example of cooperation is found in the State Department's Export Control and Related Border Security (EXBS) Program, which has supported training for Chinese licensing and enforcement officials. The EXBS effort is designed to help key source, transit and transshipment countries to establish or enhance strategic trade control systems, including border control capabilities, that meet international standards for controlling items on the control lists of the nonproliferation export control regimes, prevent the authorization of transfers to end-uses and end-users of proliferation concern, and detect and interdict illicit transfers at the border. Our EXBS cooperation with China is funded from funds appropriated for the Nonproliferation and Disarmament Fund (NDF). In addition, in coordination with the EXBS program, the Department of Energy conducts Commodity Identification Training aimed at training Chinese frontline Customs enforcement officials and technical experts responsible for assessing exports of shipments for nuclear proliferation concerns.

The Department of Energy is also actively engaged with the Chinese in areas related to physical protection for and the control and accounting of nuclear materials. In the past two years, there have been several bilateral workshops and seminars on a range of important nuclear security topics, including the highly successful Integrated Nuclear Material Security Technology Demonstration at the China Institute of Atomic Energy in October 2005. This effort has productively built upon the clear and shared interest of both countries in utilizing recognized best practices for protecting their nuclear material from potential threats of theft or diversion.

Other examples of our effort are the Container Security Initiative and the Megaports Initiative, where the Department of Homeland Security and the Department of Energy are working with China to improve detection of radiological and nuclear items at seaports.

We also believe China should join the Proliferation Security Initiative (PSI), which was created by the President to facilitate cooperation in the interdiction of nuclear, chemical and biological weapons, their delivery systems, and related technologies. The hallmark of the PSI is the close and innovative interaction between diplomacy, military, intelligence, and economic tools to combat proliferation. PSI has become an important tool to interdict shipments, disrupt networks, and hold companies accountable for their activities. Beijing has thus far been reluctant to join with the more than 80 nations participating in the PSI, citing legal concerns. It also is quite possible that Beijing feels it must take into account North Korea's likely reaction to China's participation in the PSI, a program that the North Koreans believe targets them directly. Notwithstanding any possible North Korean objection, China's commitment and participation in this program would be invaluable and we have been seeking to address Beijing's concerns, emphasizing that PSI actions are taken in accordance with states' domestic authorities and international law.

Recently, we have seen another promising development that merits mention. Certain Chinese companies that are currently subject to U.S. nonproliferation sanctions have reportedly adopted measures to ensure their adherence to China's export control laws and regulations. For example, the China North Industries Corporation (NORINCO)

reportedly has adopted an internal compliance program that will help ensure its exports are consistent with Chinese law, and has engaged the advisory services of the University of Georgia Center for International Trade and Security (which, as I understand it, has been invited to testify to this Commission). Getting NORINCO, a firm that has been sanctioned seven times since 2001, out of the proliferation business would be a very positive development and one that could serve as an example to other Chinese companies. We remain guardedly optimistic that these efforts are sincere and long-lasting.

Conclusion

Mr. Chairman, China has made much progress in the area of nonproliferation, but more needs to be done. The United States will continue to press China to implement effectively its export control regulations, eliminate loopholes, and reign in the proliferation activities of certain companies. Continued proliferation by Chinese entities to countries of concern is not in the U.S. interest, nor is it in China's interest. China's success in stopping proliferation by certain entities is critical to ensuring that sensitive items and critical technology do not end up in the hands of terrorists or other programs of proliferation concern. It is in our common interest to work together to ensure an end to such proliferation activity.